

Message Text

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TAGS: ECON, EEWT, XH, NATO

SUBJECT: ECONADS: RECENT DEVELOPMENTS IN USSR AND EASTERN EUROPE

1. ECONOMIC DIRECTORATE TRADITIONALLY PREPARED SMI- ANNUAL REPORT ON RECENT DEVELOPMENTS IN USSR AND EASTERN EUROPE FOR USE AS REFERENCE DOCUMENT AT MINISTERIALS. ALTHOUGH REPORT IS SUBMITTED TO SYG AS NOTE FROM ECONOMIC DIRECTOR RATHER THAN AGREED ECONOMIC COMMITTEE STUDY, COMMENTS FROM DELEGATIONS ARE WELCOMED. TEXT OF MAIN FEATURES SECTION OF REPORT PREPARED FOR MAY MINISTERIALS IS QUOTED BELOW, USNATO WOULD APPRECIATE WASHINGTON COMMENTS PRIOR TO NEXT ECONOMIC COMMITTEE MEETING MAY 7.

2. BEGIN QUOTE MAIN FEATURES:

I. MAIN FEATURES

IN 1974 WARSAW PACT COUNTRIES MAINTAINED MORE STABLE DOMESTIC PRICES AND EXTERNAL BALANCES THAN DID MOST INDUSTRIALIZED WESTERN NATIONS. ECONOMIC GROWTH WAS MODERATELY RAPID, ALTHOUGH SLOWER THAN IN 1973. IN EASTERN EUROPE, HOWEVER, THIS PATTERN MIGHT WELL CHANGE CONSIDERABLY IN THE NEAR FUTURE BECAUSE OF THE DELAYED IMPACT OF THE SHARP RISE IN WORLD PRICES IN 1973-74. SUCH A DEVELOPMENT MIGHT POSE SOME DILEMMAS FOR THE USSR. WHILE ITW TERMS OF TRADE HAVE
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IMPROVED DRAMATICALLY WITH DEVELOPED COUNTRIES-- COMMUNIST AS WELL AS NON COMMUNIST-- UNINHIBITED EXPLOITATION OF THIS ECONOMIC LEVERAGE ON EASTERN EUROPE MIGHT SERIOUSLY INCREASE RISKS OF ECONOMIC STAGNATION IF NOT SOCIAL INSTABILITY THERE.

2. TO DATE, EAST- WEST TRADE IS THE ASPECT OF EASTERN ECONOMIC ACTIVITY WHERE WORLDWIDE INFLATIONARY FORCES HAVE HAD THEIR GREATEST IMPACT-- GENERALLY FAVORABLE FOR THE USSR, UNFAVORABLE FOR EASTERN EUROPE. ALTHOUGH A RELATIVELY SMALL MARKET, THE WARSAW PACT AREA PROVIDED NATO COUNTRIES WITH A FAVORABLE TRADE BALANCE OF ABOUT \$2.5 BILLION IN 1974 FOR THE SECOND SUCCESSIVE YEAR. LAST YEAR THIS SURPLUS WAS EARNED ENTIRELY IN EASTERN EUROPE WHERE HARD CURRENCY TRADE DEFICITS ROSE CONSIDERABLY AS A RESULT OF STRONG DEMAND FOR WESTERN MACHINERY AND TECHNOLOGY (ESPECIALLY IN POLAND), PRICE INFLATION OF WESTERN EXPORTS, AND A RECESSION IN WESTERN DEMAND. THE SAME FACTORS LIMITED THE TRADE DEFICIT INCURRED BY NATO AND OTHER INDUSTRIAL WESTERN COUNTRIES WITH THE USSR, PARTIALLY OFFSETTING THE RAPID INCREASE IN SOVIET HARD CURRENCY EARNINGS RESULTING FROM DIVERSIFICATION OF EXPORT CAPABILITIES (E.G. IN TRANSPORT SERVICES) AND FROM HIGHER WORLD PRICES FOR SOVIET ENERGY, MATERIALS AND GOLD. ACCORDING TO THE ECE (GENEVA). THE VOLUME OF THE FOREIGN TRADE OF WARSAW PACT COUNTRIES ROSE MORE RAPIDLY WITH EACH OTHER THAN WITH THE INDUSTRIAL WEST. THE IMPROVEMENT IN ITS TERMS OF TRADE THUS ENABLE THE SOVIET UNION SIMULTANEOUSLY TO EARN ITS FIRST TRADE SURPLUS IN YEARS IN THE WEST, AND TO INCREASE ITS COMMERCIAL DEALINGS IN REAL TERMS WITH ITS ALLIES.

3. LITTLE REFLECTION OF THESE EXTERNAL STIMULI AND SHOCKS HAS YET APPEARED IN EASTERN DOMESTIC ECONOMIES, WHICH HAVE BEEN SHIELDED FROM OUTSIDE INFLUENCES BY ADMINISTRATIVE CONTROLS OVER MOST PRICES, BY THE RELATIVELY SMALL PROPORTION OF GNP ALLOCATED TO TRADE WITH NON COMMUNIST COUNTRIES, AND (IN THE CASE OF THE USSR, ROMANIA AND POLAND) BY SIZEABLE DOMESTIC ENERGY RESOURCES. POLAND HUNGARY AND ROMANIA HAVE EXPERIENCED MODERATE, SINGLE DIGIT INFLATION OF SOME DOMESTIC PRICES. THESE IMBALANCES AND THE RISING EXTERNAL TRADE DEFICITS HAVE BEEN LESS SEVERE THAN IN MOST WESTERN COUNTRIES, HOWEVER, AND DID NOT HAVE A SIGNIFICANT EFFECT ON EASTERN ECONOMIC GROWTH IN 1974.

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4. SOVIET ECONOMIC GROWTH SLOWED DOWN LAST YEAR TO ABOUT 3PCT IN TERMS OF GNP AND MAY ATTAIN AN AVERAGE OF THE ORDER OF 4 PCT OF THE YEARS 1971-1975-- CREDITABLE BY WESTERN STANDARDS THOUGH SHORT OF THE OVER 5PCT RATE IMPLIED BY THE FIVE YEAR PLAN. EASTERN EUROPE ON THE WHOLE IN 1974 MAINTAINED A RAPID EXPANSION THAT SEEMS TO PLACE MAJOR FIVE YEAR PLAN TARGETS WITHIN REACH. IN POLAND HOWEVER, DESPITE STRONG OVERALL PERFORMANCE, DISTURBANCES WERE REPORTED BECAUSE OF MEAT SHORTAGES. THE DECISIVE FACTOR IN THESE DEVELOPMENTS APPEARS TO HAVE BEEN THE CRITICAL AGRICULTURAL SECTOR. POOR OR MEDIOCRE HARVESTS CONSTRAINED POLISH MEAT SUPPLIES AND HANDICAPPED OVERALL SOVIET PERFORMANCE WHILE AN EXCEPTIONALLY GOOD CROP APPARENTLY ACCEL-

ERATED GROWTH IN EAST GERMANY.

5. IN THE FUTURE, HOWEVER, EASTERN ECONOMIC GROWTH WILL PROBABLY BE AFFECTED TO A GREATER DEGREE BY EXTERNAL TRADE BALANCES, WHICH PROMISE TO BE INCREASINGLY FAVORABLE FOR THE USSR AND UNFAVORABLE FOR EASTERN EUROPE. NEW ORDERS FOR WESTERN EQUIPMENT HAVE CONTINUED TO ACCELERATE IN 1974-75 AND SHOULD HAVE A GRADUALLY INCREASING IMPACT ON INVESTMENT AND GROWTH. IN EASTERN EUROPE, HOWEVER, THE TERMS OF TRADE WITH THE USSR HAVE RECENTLY BEEN REDUCED BY AN INCREASE IN SOVIET ENERGY AND MATERIALS PRICES THAT TRANSMITS PART OF THE EARLIER RISE IN WORLD PRICES. THIS PRESSURE WILL PROBABLY LEAD MOST EAST EUROPEAN COUNTRIES TO DIVERT FURTHER COMMERCE FROM THE WEST TO THE USSR AND TO SLOW DOWN PROGRAMS FOR INDUSTRIALIZATION AND CONSUMER WELFARE. THE CONSIDERABLE ECONOMIC LEVERAGE THAT WORLD PRICE MOVEMENTS HAVE GIVEN THE USSR OVER ITS ALLIES MAY ACCORDINGLY BE EXERCISED WITH DISCRETION AND BE AIMED AS MUCH AT POLITICAL OBJECTIVES-- E.G. COMECON INTEGRATION-- AS AT COMMERCIAL ADVANTAGE.

END QUOTE MAIN FEATURE. BRUCE

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